MNCs Are Allowed More Flexibility In The Choice Of Entry Mode In China

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Abstract

This study identifies how MNCs (Multinational Corporations) are allowed more flexibility in the choice of entry mode in China, in terms of three dimensions—organizational form, structure, and industry selection, by comparing data on these three dimensions during 1980-1994 with data during 1995-2003 and analyzing incremental change of government policy. Results show that MNCs are allowed more flexibility in organizational form and industry selection. However, more flexibility in structure is conditional due to the deficiency of data collected. In addition, new findings are obtained that joint ventures remain the primary entry mode choice, the number of joint partners and joint ventures between MNCs increases, and many MNCs change their operation mode after initial entry in terms of certain rules.

Keywords:

entry mode, flexibility, organizational form, structure, government policy, incremental change

Introduction

With the expansion of firms to international market, choice of entry mode becomes increasingly important. Uppsala School advocates that the process is gradual because of the inborn risks (different political, economic, cultural, and market systems) existing in host countries (e.g. Johanson and Vahlne1977). That is, risk, resource commitment, control and profit potential increase step by step according to the sequence of "export via an agent—sales subsidiary (acquisition of the agent or organized around employees of the agent)—local production"(Johanson and Vahlne 1977). According to Chu and Anderson (1992 in Pan and Tse 2000), this process is simplified as "from export to wholly owned

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subsidiaries". Meanwhile, Pan and Tse (2000) develop another model, pointing out that this process is hierarchical: "The first level is between equity and non-equity modes. Within non-equity modes, contractual agreements are compared to export. Within equity modes, wholly owned subsidiaries are compared to equity joint ventures (EJVs)."

Based on the entry modes, market entry strategies are developed. Although there exist a variety of forms, focuses are different during different periods. In the 1960s, differentiation of exporting and FDI (Foreign Direct Investment) is focused. In the 1970s, licensing, franchising and subcontracting are added to the strategic options. In the 1980s, mergers and acquisitions (M&As) are refocused (Buckley and Casson 1998).

Generally, larger firms with more multinational experience are more likely to choose investment modes, and countries with higher market potential are more likely to attract investment modes. However, investment modes may be chosen by larger multinational firms even in lower potential countries (tend to be developing countries). In this way, MNCs may secure opportunity for higher returns resulted from greater market imperfections that cannot be obtained in high potential countries (Agarwal and Ramaswami 1992).

Since 1979, China has engaged in export-driven mercantile policies, which meant international trade began to be encouraged. At the same time, China began to attract FDI with the Open Door policy of 1982. Although the process is slow before 1992, FDI in China has increased rapidly since then, due to the promulgation of "Provisions for the Encouragement of Foreign Investment" in 1986 and 1987 (Chadee and Qiu 2001). However, many market imperfections still exist in China because firm-government related system had resulted in fragmented economy with few dominant firms and little competition before the economic reform (Boisot and Child, 1996, in Child and Tse, 2001). Nevertheless, MNCs are competing for entering Chinese market due to the encouragement of government policies and the attractiveness of large sized population.

Child and Tse (2001) make a set of propositions on the development of international business in China through the analysis of China's economic transition. The second proposition (P2) suggests that MNCs can choose all types of entry modes with the marketization of and gradual compliance with international standards of China's economy. Derived from this proposition, a hypothesis is formed and will be tested formally. Thus, the hypothesis, research question and research objective are as follows.

Hypothesis: MNCs are allowed more flexibility in their choice of entry mode in China.

Research Question: How are MNCs allowed more flexibility in their choice of entry

mode?

Research Objective: To identify MNCs' flexibility in the choice of entry mode, including the choice of organizational form, structure and industry.

In the following, this paper will begin with a review of literature. Then the methodology will be discussed. After the research findings and discussion, the contributions and limitations of this study will be concluded.

Literature Review

How firms choose market entry mode is an important issue. Many researches have focused on factors that influence entry mode choice. Among them, Dunning's comprehensive framework is used with the most frequency as the basis of explaining entry mode choice. For example, choice between joint venture and sole venture (Kogut and Singh 1988), licensing and sole venture (Caves, 1982, Davidson and McFetridge, 1985, in Agarwal and Ramaswami, 1992), and ratio of acquisition to total subsidiaries (Wilson, 1980, in Agarwal and Ramaswami, 1992). The influence of market entry mode has also been researched, e.g. its impact on profitability and market share (Pan, Li and Tse 1999).

Entry modes typically include export, licensing arrangement, joint venture and wholly owned subsidiary (Tse, Pan and Au. 1997). Except for export, they are researched with most frequency (e.g. Hill, Hwang and Kim 1990). All of these modes involve resource commitments, risk/return and control. These indices are positively related. That is, low resource commitments imply low risk/return and low control, while high resource commitments mean the other two are high. These indices of exporting and licensing are low, while those of wholly owned venture are high and those of joint venture are between (Agarwal and Ramaswami 1992).

Another approach divides the entry modes into equity and non-equity. Equity modes differ from non-equity modes in that they require establishment and direct management of independent organizations, as well as interaction with local partners beyond contracts (e.g. Anderson and Gatignon 1986). In addition, the geocentric approach considers these subsidiaries interdependent to form a network (Kim and Hwang 1992).

Although export and other non-equity modes are less risky than wholly owned and joint ventures, the result is reverse in China. Pan (1996) contends that equity modes are easier and less risky due to macro-economic policies in China. In other words, host countries may dictate inflexible modes through policy enforcement. This also explains to some

extent why joint ventures are the oldest and popular form in China (Davidson 1987; Eiteman 1990; Beamish 1993).

However, although the joint venture law of 1979 requires that the equity share of the foreign JV partner should be no less than 25%, exceptions abound in practice (Shan 1991). In addition, non-equity or CJVs (cooperative joint ventures) represented the most popular form of entry mode even prior to the establishment of relevant law in 1988 (Tao, 1988, in Shan, 1991). In other words, all forms of entry mode become informal common law before the formal law is approved.

Furthermore, in ten years since the promulgation of the first joint venture law in 1979, China has announced over 500 laws, provisions and regulations with regard to foreign ventures, let alone the recent years. It is just these laws and their recent revisions that are encouraging MNCs to enter China and allowing them to choose entry modes more flexibly.

Since the objective of this study is to identify MNCs' flexibility in the choice of entry mode including choice of organizational form, structure and industry, the following will define the three dimensions. As for *flexibility*, the definition is not fixed because of the different dimensions.

Organizational Form

Many different approaches are used to define and measure this term.

Some researchers hold that any type of entry mode can be categorized to either acquisition or greenfield investment. The former means using funds to purchase the facility second-hand as a going concern, while the latter suggests investing the funds to construct a new facility. They also point out the effective approach to determine market entry mode, by measuring the profitability of each and then choosing the most profitable one, whether the *organizational form* is wholly owned or joint venture, greenfield investment or acquisition.

Hagedoorn and Narula (1996) divide alliance form in two basic categories, according to the involvement of an agreement: The first concerns equity sharing, in particular joint ventures and jointly owned research corporations; The second is contractual alliances that cover a relatively large group of partnerships without equity sharing, such as joint development agreements, joint research pacts, cross licensing, second-sourcing agreements, mutual second-sourcing, and R&D contracts.

Although researchers have successfully used *transaction cost* to analyze the choice

of *organizational form*, which is also termed as *ownership*, few of them focus on the government restrictions on MNCs' choices of *organizational form* (Gomes-Casseres 1990). However, this point is so important in China that a MNC would rather choose joint venture form even the transaction cost of choosing wholly owned form can be lower. Another approach of analyzing *organizational form*-- the bargaining power model, makes up for the deficiency in that it takes the host government's restrictions into consideration. While the transaction cost approach solves the problem of what *organizational form* MNCs want, the bargaining power approach answers the question of what *organizational form* they can obtain in fact (Gomes-Casseres 1990). As a result, the two approaches are complementary.

Thus, organizational form here refers to the form of entry mode, which also is termed as ownership, or partnership (only in alliance form), mainly including wholly owned and joint venture, merger and acquisition, licensing as well as agents.

If the government restrictions are not considered, the MNC's choice of organizational form is actually the balance between "need for resources" and "need for control" (Stopford and Wells, 1972, in Gomes-Casseres, 1990). The difference between joint venture and wholly owned venture is especially pointed out. That is, the choice of the former demonstrates the need for resources to a greater extent, while the selection of the latter indicates more need for control (Gomes-Casseres 1990). In addition, EJVs and wholly owned ventures would have higher market shares and profitability than non-equity forms such as CJVs (Pan, Li and Tse 1999). Therefore, MNCs entering through non-equity forms are at a disadvantage due to the relative lack of control.

The choice of organizational form is also based on measuring costs and benefits, which leads to "ownership preference" according to Gomes-Casseres (1990). Furthermore, different degrees exist among even the same kind of organizational form. For instance, one of the two MNCs that both choose wholly owned ventures may prefer this form more intensely than the other.

Gomes-Casseres (1990) contends, on the other hand, that although "preference ranking" is also valid when the government restrictions are considered, the relative bargaining power of MNC and government becomes the key determinant in choosing organizational form. That is, the organizational form is chosen after balancing the importance of firm factors and government factors. For example, a firm ranking wholly owned form significantly higher than a joint venture will be less likely to give in on the decision of organizational form than a firm which, although still prefers wholly owned form, sees a joint venture as a more likely alternative.

As a result, *flexibility* in the dimension of *organizational form* is defined as the government policies in China are allowing MNCs to choose diversified organizational form.

Structure

The basic tone of this study is MNCs' standpoint. Thus, *structure* here refers to the share of foreign ownership, which is referred by Chadee and Qiu (2001) as the level of ownership. They further point out two ways of definition. One is to identify majority or minority. Majority share means the foreign partner possesses more than 50% of the total share (Pan 1996). In other words, 50% is considered the criteria of distinguishing between majority and minority. Also, there often exist situations of 50/50%, called equal share, some of them are resulted from government regulations in China. Therefore, the key decision to MNCs is whether to go for a minority, an equal, or a majority share of ownership. This classification is also applied in other researches. For example, Contractor (1990 in Pan 1996) holds that the difference between a 49% and a 50% share is distinctive, compared with the difference between a 25% and a 26%. In addition, Pan (1996) suggests that the partner contributing more to the initial capital will prefer a majority, while the same partner will prefer a minority of the share if the total investment amount is high. Shan (1991) also concludes that the foreign firm assumes a minority share of ownership when the investment amount increases and when the duration of the venture decreases.

The other way is to define the share of ownership as "the proportion contributed by the foreign partner to the total cost of the project", which can "range from minimum of 25% of equity share to a theoretical maximum of 99.9%" according to Chinese Law (Chadee and Qiu 2001).

This paper will apply the first way of definition. That is, the share of foreign ownership includes majority, minority or equal. Thus, *flexibility* in the dimension of *structure* means that MNCs can choose majority, minority or equal share flexibly. However, this dimension cannot apply to wholly owned venture.

Industry selection

Dunning (1980, 1988) proposes the eclectic framework on cross-border business activities, regarding industry selection as one of the factors that could influence these activities. In other words, industry selection should be ascribed to determinants in the choice of entry mode.

Hagedoorn and Narula (1996) conclude that the choice of entry mode varies with the industry sectors, e.g. Joint ventures are disproportionately represented in relatively mature industries, while contractual alliances, in so-called high-tech industries. In addition, Pan

and Tse (2000) point out that firms in industries of high advertising intensity and of high asset turnover prefer equity modes to non-equity modes. Moreover, Harrigan (1988 in Tse, Pan and Au 1997) finds that firms in aerospace industry have a higher possibility to choose joint ventures than those in the farm equipment industry. Because barriers of entry and exit costs are substantially higher for firms in large-scale operation industries, they may seek alliances with non-PRC firms to reduce the risk and to share the resources input. At the same time, they would prefer equity-based modes since they consider operation control important. As implied by these researches, industry selection should be defined as a rational process that can match the industry with appropriate entry mode.

In the early 1980s, industry selection for MNCs entering in China is limited to industrial and construction sector. However, in the 20 years since then, the scope has been expanded in major industries of China's national economy, such as agriculture, oil exploration, transportation, telecommunications, commerce, trade, finance and banking. Thus, China's whole industrial structure has improved. For example, many sectors have begun to change from being labor-intensive to technology-intensive (http://english.peopledaily.com.cn/50years/achievement/19990910A116.html).

Because of deregulation in areas such as energy, telecommunications, financial services, automotive and service sectors (Hsieh and Jen 2001), MNCs can choose flexibly to enter these industries, which implies *flexibility* in the dimension of industry selection. This definition is expanded by Yang and Lee (2002), who point out that a new government policy was established to provide foreign corporations with more flexibility in selecting industries to be entered, such as: the joint stock holding companies (e.g. investment in the manufacturing industry), the investment company (e.g. banking and bond industry), the mutual fund institutions (e.g. financial management industry), and foreign trade businesses. Thus, *flexibility* in industry selection means MNCs can enter more industries, which were exclusive to local firms or restricted to joint venture form.

Methodology

The research approach adopted in this study is deductive, meaning that a hypothesis is proposed at the beginning and then is tested through quantitative or qualitative analysis. This approach is used most commonly in scientific research (Saunders, Lewis and Thornhill 2003). Hypothesis will be tested using a longitudinal sample of 34 MNC activities in China between 1980s and 2003, since China has been going through major economic and political changes since 1979, and the recent activities may predict the future trends. Furthermore, this research will use "pooled cross-section—time series methods" (Chadee and Qiu 2001). That is to say, these data will be divided in terms of time section. Thus, secondary data will be collected and analyzed.

Data Collection

At the beginning, I wanted to look for coded information on foreign operations between 1980s and 2003 from the China Business Review, which is a major bimonthly trade magazine published by the U.S.-China Business Council, an independent business association headquartered in Washington D.C. However, what can be found is not data related to this research but macroeconomic data. For example, China was the second largest recipient of foreign investment (next to the U.S.), with inflow of US$34 billion in 1994 and 1995, US$42.6 billion in 1996, and US$45.3 billion in 1997. Fortunately, as large companies, almost all the MNCs have their own website introducing their first entry and development in China. As a result, the data is based on these websites as well as news releases about business operations in China.

Data Set

According to the information founded, I firstly coded it into raw data showed in the appendix, which contains data on three dimensions of the research hypothesis. The inter-coder reliability was high (about 98%) because most of the items coded were factual and few subjective judgements are involved. Secondly, I arranged the coded information in a tabular form in terms of company name, year of activities, and three dimensions defined in literature review part (Table 1). Then, all these data are divided in two time sections, revising Table 1 to Table 2. One reason of the period division is relative lack of relevant information during 1980s. Another reason is that although FDI has increased most rapidly after 1992 (Chadee and Qiu 2001), the effect emerged actually around 1995. The most important reason, however, is the promulgation of "Regulations for Guiding the Direction of Foreign Investment" and "Catalogue for Guiding Foreign Investment in Industries" from 1995. The former categorized the industries into those that are *encouraged, permitted, restricted and prohibited* for foreign investment. The latter listed the encouraged, restricted and prohibited categories. Those not listed belong to the permitted category. The prohibited category refers to industries which are completely not allowed foreign investment. The restricted category is subject to more stringent government approval requirements and further restrictions in terms of organizational form and/or structure than the encouraged and permitted categories. Consequently, the first section is from 1980 to 1994, the second is from 1995 till 2003. Naturally, data will be analyzed in terms of the two different periods separately at first, and then respective results will be compared according to three dimensions of the research objective. In this way, "more flexibility" in the research hypothesis can be tested.

Sampling

As for the sampling of this research, only joint venture, wholly owned venture, representative, merger and acquisition are mentioned. However, this does not mean that other entry modes are not considered. Exporting is the primary and original step

TABLE 1

Company	Year	Organizational Form	Structure(%)	Industry
Nokia	1994	JV	N	Telecommunications
	1998	W		
	2000	JV	N	
	2003	M	60	
IBM	1980's	R		Computer
	1992	W		
	2000	JV	70	
3Com	2003	JV	49	Network
Alcan	2002	JV	50	Aluminum
Volkswagen	1984	JV	50	Automotive
Mitsubishi	2003	JV	55	Acrylic fiber
Benckiser	1996	JV	60	Detergent
JVC	2000	JV	70	Deflection yokes
Motorola	1987	R		Telecommunication
	1992	W		
NEC	1989	JV	N	Manufacturing
	1996	W		
	2002	JV	25	
Toshiba	1995	JV	40	Electronics
FedEx	1999	JV	N	Express transportation
Matsushita	2002	JV	25	Manufacturing
Kingston	2001	JV	80	Computer
Siemens	1990	JV	N	Telecommunication
	1992	JV	N	
	1994	W		
GM	1997	JV	50	Automotive
Honda	2001	M	50	Automotive
Marconi	2000	T	Majority	Telecommunication
Samsung	2001	JV	49	Electronics
Rhodia	2001	JV	70	Chemistry
Autoliv	1995	JV	30	Manufacturing
BP	2002	JV	40	Oil exploration
HongKong Lika-shing	2000	A	50	Medicine
Lonza	1999	JV	Majority	Chemistry

TABLE 2

Period	Organizational Form	Structure(%)	Industry	Company
1980-1994	JV	N	Telecommunications	Nokia
	R		Computer	IBM
	W		Computer	
	JV	50	Automotive	Volkswagen
	R		Telecommunications	Motorola
	W		Telecommunications	
	JV	N	Manufacturing	NEC
	JV	N	Telecommunications	Siemens
	JV	N	Telecommunications	
	W		Telecommunications	
1995-2003	W		Telecommunications	Nokia
	M	60	Telecommunications	
	JV	N	Telecommunications	
	JV	70	Computer	IBM
	JV	49	Network	3Com
	JV	50	Aluminum	Alcan
	JV	55	Acrylic fiber	Mitsubishi
	JV	60	Detergent	Benckiser
	JV	70	Deflection yokes	JVC
	W		Manufacturing	NEC
	JV	25	Manufacturing	
	JV	40	Electronics	Toshiba
	JV	N	Express transportation	FedEx
	JV	25	Manufacturing	Matsushita
	JV	80	Computer	Kingston
	JV	50	Automotive	GM
	M	50	Automotive	Honda
	T	Majority	Telecommunication	Marconi
	JV	49	Electronics	Samsung
	JV	70	Chemistry	Rhodia
	JV	30	Manufacturing	Autoliv
	JV	40	Oil exploration	BP
	A	50	Medicine	HongKong Lika-shing
	JV	Majority	Chemistry	Lonza

TABLE 3

Period	Organizational Form	Structure(%)	Industry	Company
1980-1994	JV	N	Telecommunications	Nokia
	R		Computer	IBM
	W		Computer	
	JV	50	Automotive	Volkswagen
	R		Telecommunications	Motorola
	W		Telecommunications	
	JV	N	Manufacturing	NEC
	JV	N	Telecommunications	Siemens
	JV	N	Telecommunications	
	W		Telecommunications	
1995-2003	W		Telecommunications	Nokia
	M	Majority	Telecommunications	
	JV	N	Telecommunications	
	JV	Majority	Computer	IBM
	JV	Minority	Network	3Com
	JV	50	Aluminum	Alcan
	JV	Majority	Acrylic fiber	Mitsubishi
	JV	Majority	Detergent	Benckiser
	JV	Majority	Deflection yokes	JVC
	W		Manufacturing	NEC
	JV	Minority	Manufacturing	
	JV	Minority	Electronics	Toshiba
	JV	N	Express transportation	FedEx
	JV	Minority	Manufacturing	Matsushita
	JV	Majority	Computer	Kingston
	JV	50	Automotive	GM
	M	50	Automotive	Honda
	T	Majority	Telecommunications	Marconi
	JV	Minority	Electronics	Samsung
	JV	Majority	Chemistry	Rhodia
	JV	Minority	Manufacturing	Autoliv
	JV	Minority	Oil exploration	BP
	A	50	Medicine	HongKong Lika-shing
	JV	Majority	Chemistry	Lonza

TABLE 4

Period	Organizational Form	Structure(%)	Industry	Company
1980-1994	JV	N	Telecommunications	Nokia
	R		Computer	IBM
	W		Computer	
	JV	50	Automotive	Volkswagen
	R		Telecommunications	Motorola
	W		Telecommunications	
	JV	N	Manufacturing	NEC
	JV	N	Telecommunications	Siemens
	JV	N	Telecommunications	
	W		Telecommunications	
1995-2003	W		Telecommunications	Nokia
	M	Majority	Telecommunications	
	JV	N	Telecommunications	
	JV	Majority	Computer	IBM
	JV	Minority	Network	3Com
	JV	50	Manufacturing	Alcan
	JV	Majority	Chemistry	Mitsubishi
	JV	Majority	Chemistry	Benckiser
	JV	Majority	Chemistry	JVC
	W		Manufacturing	NEC
	JV	Minority	Manufacturing	
	JV	Minority	Electronics	Toshiba
	JV	N	Express transportation	FedEx
	JV	Minority	Manufacturing	Matsushita
	JV	Majority	Computer	Kingston
	JV	50	Automotive	GM
	M	50	Automotive	Honda
	T	Majority	Telecommunications	Marconi
	JV	Minority	Electronics	Samsung
	JV	Majority	Chemistry	Rhodia
	JV	Minority	Manufacturing	Autoliv
	JV	Minority	Oil exploration	BP
	A	50	Chemistry	HongKong Lika-shing
	JV	Majority	Chemistry	Lonza

Note: JV-joint venture; W-wholly owned venture; M-merger; R-representative office;
T-takeover; A-acquisition; N-not found.

to enter a foreign market, as mentioned in the introduction part. But in the sense of the two dimensions defined previously—organizational form and structure, it cannot be measured. Together considering that the wholly owned venture also cannot be measured in the dimension of structure, it can be concluded that the entry mode can be considered in the research sample only if at least two dimensions of the three can be measured. As for licensing, some joint ventures adopt this way of production. Because franchising is mainly centralized in some industries such as food and retailing, it is also not taken into consideration in data collection. Agents and distributors of MNCs would be replaced by sale subsidiaries (representative offices) quickly, due to MNCs' capabilities in resisting risks and needs in controlling. In addition, some joint ventures are the result of alliances. Thus, except the two early forms in the theory of entry mode sequence (Johanson and Vahlne 1977), almost all entry modes are considered in fact.

Findings and Discussion

Data analysis

Organizational form

From Table 2, we can see that during 1980-1994, there exist 5 joint ventures, 2 representative offices and 3 wholly owned ventures. It demonstrates that joint ventures, as the primary organizational form in the early days of China's opening, account for 50% of entry mode MNCs chose in the sample. This also proves the validity of China's 1979 Law on Joint Ventures. In addition, representative offices and wholly owned ventures began to emerge. In the sample, they account for 20% and 30%, respectively.

During 1995-2003, there are 18 joint ventures, 2 wholly owned ventures, 2 mergers, 1 acquisition and 1 takeover. This is to say, joint ventures not only still remain the majority of the entry mode, but also increase to 75% of the whole entry in the sample. Moreover, three new types of organizational form have begun to appear—merger, acquisition and takeover. Although wholly owned ventures still emerge, the rate is so slow that it only accounts for 8% of the whole during this period. At the same time, representative office is almost replaced by other types of organizational form. This can support the theory developed by Johanson and Vahlne (1977), who consider "sales subsidiary—local production" as part of the entry mode sequence, since representative office is set up mainly to marketing.

In general, the dimension of *organizational form* in the hypothesis of this study can be supported to be of flexibility in that MNCs have chosen more types organizational form during the second period compared with the first period in the research sample.

This trend can also be illustrated by individual sample. For example, Nokia only set up

joint venture during 1980-1994, while entered China through wholly-owned venture, joint venture and merger during 1995-2003. IBM set up representative office and wholly-owned venture during 1980-1994, but also set up joint venture during 1995-2003. Similarly, NEC only had joint venture during 1980-1994, during 1995-2003, however, established joint venture as well as wholly-owned venture.

More flexibility in *organizational form* results from the incremental change of China's government policy. After the joint venture law of 1979, the government launched law of wholly foreign-owned enterprises in 1986, allowing MNCs to establish wholly-owned ventures in certain industries. In addition, the government promulgated law of merger and acquisition in 2003 and revised it in 2006, making legal M&As of Chinese domestic companies by MNCs. The most prominent are "Regulations for Guiding the Direction of Foreign Investment" issued in1995 and revised in 2002, and its appendix "Catalogue for Guiding Foreign Investment in Industries" launched in 1995 but revised in 1997, 2002, 2004 and 2007 respectively (thus they are called the Catalogues). As stated previously, the Catalogues stipulate industries in terms of encouraged, restricted or prohibited to foreign investment. The investment in encouraged category often enjoys the right to establish wholly foreign-owned subsidiary, while that in restricted category is often limited to joint venture. Thus, the gradual change of China's policy related to investment form has allowed MNCs to be more flexible in *organizational form*.

Structure

In order to analyze the data conveniently, table 2 is revised in the dimension of structure according to its definition in literature review part. That is, share of ownership more than 50% is changed to majority, less than 50% is revised to minority, 50% remains unchanged. The result can be shown clearly in table 3. However, there exist two deficiencies here. From table 3, we can see that only one structure during the first period is found (50%). However, from another standpoint, it may be explained by that share of foreign partner in joint ventures in the early Opening days is not of much difference. In other words, structure during 1980-1994 may be relatively inflexible. Government regulations may limit the maximum share in order to reform without instability, or the MNCs may still suspect practicality and validity of Opening Door in China and invest cautiously. The second defect is this dimension cannot apply to wholly owned venture, which is an important form in the early opening days and may become a main form in the future because its high control and high profitability. Thus, the following will analyze structure in joint venture, merger, acquisition and takeover during the second sample period.

During 1995-2003, data found include 20 structures. Among them, *majority* share accounts for 45% (9/20), *minority* share accounts for 35% (7/20), *and equal* share

accounts for 20% (4/20). Since none of them reaches half of the whole, they are not distributed disproportionately. In other words, structure is flexible.
If the relative inflexibility in structure during the first sample period can be proved true by data, which has not been found in fact, then the structure dimension of this research hypothesis can be tested to be more flexible.

This can also be explained by the revision and development of China's policy especially the Catalogues. In both encouraged and restricted categories, foreign investment in certain industries is only allowed to have minority share. For example, the 1995 Catalogue stipulates that construction and management of city subway and light track is encouraged but with the state assets taking the holding or leading position, and that complete limousine and complete motorcycles are restricted with the state assets taking the holding stock or leading position. Foreign investment in other industries not specifically illustrated in the restricted categories is allowed to have majority share. Furthermore, foreign investment in a few encouraged industries is not allowed to set up wholly-owned venture, i.e. allowed to have majority share. For example, the 1995 and 1997 Catalogues regulate that mining of copper, lead and tin is encouraged but wholly foreign-owned enterprises are not allowed. Generally speaking, since 1995, China's policy regarding ownership regulation has allowed more flexibility in *structure*.

Industry
Data on industry in table 3 is revised and table 4 is produced. During 1980-1994, 6 of 10 entries are into telecommunications, 2 are into computer industry, one for automotive industry and one for manufacturing. Obviously, telecommunication industry is what MNCs competed to enter. On the one hand, telecommunication industry itself was in the developing phase of its life cycle. Huge market was needed imperatively to support its development. On the other hand, MNCs were not allowed to enter the potentially huge market and enjoy the benefit from imperfections of telecommunication industry in China, due to the monopoly of Chinese government. Accordingly, once deregulation, foreign firms of this industry would never give up. As the national industry, which many SOEs are located in, automotive and manufacturing in China can provide MNCs with low labor cost and production base. However, to reform with stability, Chinese government is bound to protect it at the beginning and open it incrementally.

During the second period, more industries are involved, including network, chemistry, electronics, and even express transportation, a pillar industry of a country. In addition, entering in telecommunication, computer and automotive industries remains popular.
Data on industry should be selected with intention, although it hadn't in fact. As a result, national economic industries such as agriculture, transportation, commerce, trade, finance and banking are not mentioned although telecommunication is paid much attention and

oil exploration is mentioned. Moreover, the result cannot prove the common sense that industry selection was limited to industrial and construction sector in the early 1980s, because the first sample period divided in this research contains the whole 1980s and the early 1990s.

Despite the weakness mentioned above, more flexibility in industry selection still can be supported according to the previous definition. This is also the result of policy change in China. In the Catalogues, more and more prohibited or restricted industries are open to foreign investment, having upgraded to permitted and even encouraged categories. For instance, the 2002 Catalogue, revision of the 1997 Catalogue, changed motor vehicle and motorcycle engine manufacturing from restricted category to encouraged category, increased encouraged industries from 186 to 262, and decreased restricted industries from 112 to 75.

Company

In recent years, MNCs have accelerated their large investment in China, especially the share holding companies. From table 1, we can see such companies as Nokia, Toshiba, Siemens, and IBM. They are the highest form of foreign investment, besides investment and reinvestment, their responsibility also includes product agency, the training of personnel, providing information and supplying funds.

In addition, their entry mode strategies are changing and diversified. Before 1992, most MNCs merely set up representative offices in China. But since then, they have shifted to establishing production bases. In the raw data showed in the appendix, IBM set up representative offices in Beijing and Shanghai in 1980s, while wholly-owned venture (IBM China Company Limited) in 1992. Another example is Motorola, which set up representative office in Beijing in 1987 while wholly owned venture (Motorola China Electronics Ltd.) also in 1992. Some MNCs set up joint ventures based on their wholly owned ventures. For instance, the joint venture between IBM China Company Limited and China Great Wall Shenzhen Co., Limited (a subsidiary of Chinese company Great Wall) was set up in 2000. Sometimes, two foreign companies ally to form joint ventures, e.g. Shanghai Bell (the subsidiary of Alcatel in China) and Samsung set up joint ventures in 2001. In this way, the two partners can reduce risk that may be caused by special relationship with SOEs and further with government in China. All of these cannot represent thoroughly the trend of entry mode development. With the resurge of merger, acquisition and takeover, diversification of entry mode strategies to China has been intensified. In the raw data, we can see Honda's merger (2001) with Sundiro and Tianjin Motors, Nokia's unique merger of its four original joint ventures in China (2003), Marconi's takeover of Nokia's joint venture (2000), and Hongkong Lika-shing's acquisition of the joint venture between Tongrentang, Hutchison and Jingtai. These data

also reveal that an entry mode strategy tends to involve over two partners with the advent of 21 century.

Further discussion

Although the initial entry mode should inform the strategic intention of a MNC, it may be modified over time due to the changing market conditions or the MNC's perception of the changes (Mintzberg and Waters, 1985, in Shan, 1991). Therefore, it is not unusual for MNCs to modify their initial entry mode after some experiences in China.

One of the important reasons is the gradual improvement of government policies. China has made and is making various changes to its policies, laws and regulations. For example, stipulated by the 2002 Catalogue, certain industries changed from restricted or prohibited categories to encouraged or permitted categories, in practice, however, foreign investment in some of these industries including distribution, financial services and telecommunications will still be restricted by any other relevant industry-specific national regulations. These overriding regulations may set high entry barriers for foreign investment in the "liberalized" industries.

Although there exist inconsistencies in the application and enforcement of the laws and regulations (Hsieh and Jen 2001), and many market-protecting rules remain in place, China's continued economic reform will grant MNCs more commercial selection.

Under other circumstances, previous frustrations in China make MNCs change their initial entry mode. MNCs are less likely to give up Chinese huge market than smaller companies in face of failure. Consequently, they change entry mode after frustration. For instance, PepsiCo's joint venture in Sichuan, a province in the southwest of China, failed because of management problem. However, this joint venture was among the most profitable Pepsi bottlers in China. By 2001, it had made cumulative pre-tax profits of Rmb236million (US$28.8million), of which PepsiCo received around
Rmb46 million (www.taipeitimes.com/news). As a result, PepsiCo would look for a new partner (partner selection is an important dimension of entry mode although it hasn't been discussed in this research), or set a wholly owned venture based on Sichuan market.

The percentage of wholly owned ventures has been rising. There were only 184 wholly owned ventures in 1987. By 1990, however, this form of ventures has increased twelve-fold to approximately 2,000 (People's Daily, 1990, in Shan, 1991). On the other hand, Beamish (1993) contends that Chinese government did not encourage private companies to form joint ventures with foreign partners. Instead, one or more state owned enterprises comprise the Chinese partner of most joint ventures in China. This is also shown in the research raw data. However, as stipulated by its WTO membership, China relaxed some

of the strict rules on joint ventures that previously forced MNCs to tie up with a Chinese partner. Thus, the trend of increasing wholly owned ventures is intensified as foreign firms gain greater autonomy. This trend has also been illustrated by Vanhonacker (1997).

Regardless of this trend, joint venture remains the primary entry mode in China, as demonstrated in this study. This may prove that the change of Chinese policies and regulations is incremental.

Conclusion

The findings suggest that this study achieved its main objective. Firstly, this study tested a hypothesis based on previous literature and identified that MNCs are allowed more flexibility in the choice of entry mode in China. This identification involves three dimensions of the entry mode choice, which have been defined according to previous literature. Thus, the identification of flexibility in any one dimension can support the hypothesis and testify part of it. Although flexibility of *structure* dimension is proved under the condition that data before 1995 can reveal the relative inflexibility of structure compared with corresponding data after 1995, the main stream cannot be affected because only joint venture can be applied to *structure* in the sense of "more" *flexibility* (Few of mergers, acquisitions and takeovers that apply to structure dimension emerged before 1995).

Secondly, this study explained how MNCs are allowed more flexibility in the choice of entry mode in China by analyzing the gradual change of ownership regulations since the Opening Policy, especially "Catalogue for Guiding Foreign Investment in Industries". Joint venture (JV) between MNCs and State-owned Enterprises (SOEs) was allowed for the first time in 1979. Wholly-owned subsidiary (WOS) was permitted for the first time in 1986. However, a lot of industries were still closed to foreign investment. Step by step, some were opened for WOS while some were only opened for JV with or without stipulating the SOE should hold majority share. The Catalogues made clear which industries were encouraged, which were restricted, and which were prohibited, meaning the further development of ownership deregulations. Nevertheless, some industries were downgraded from encouraged to restricted or even to prohibited categories. Moreover, other industry-specific regulations can make effect and may be taken priority over the Catalogues. Thus, ownership laws and regulations in China are complex. It is necessary for MNCs to carefully estimate which entry mode choice is advantageous under certain circumstances.

We adopted cross-section time approach in our analysis to show that entry mode during the second period (1995-2003) can be chosen with more flexibility than that during

the first period (1980-1994). By contrasting their organizational form, structure and industry selection, as well as the raw data of this study, we obtained some new findings. Joint venture remains the primary entry mode choice during 1995-2003. In addition, the organizational structures of MNCs' subsidiaries in China become more complex, as the number of joint partners increases and joint ventures resulting from alliances between MNCs grow. Furthermore, Table 1 also suggests that many MNCs, such as Motorola and IBM, chose representative offices at the beginning, and then changed to local production in the form of wholly owned or joint ventures. This sequence of entry is consistent with Johanson and Vahlne's theory (1977) about entry mode choice mentioned in the introduction part.

This study provides insights for MNCs that are ready to enter China. Since equity modes are easier and less risky than non-equity modes due to macro-economic policies in China (Pan 1996), the emphasis should be the choice between joint venture and wholly owned subsidiary. Although the main stream is joint venture, the trend toward wholly owned venture is growing. This can be explained by theory on level of resource commitment, risk/return and control mentioned in literature review part (Agarwal and Ramaswami 1992).

There are a number of limitations in the study. Firstly, the study is limited in its scope. The dimensions of identification can be expanded in practice. For example, the original country of a MNC and partner selection can form the other two dimensions that can identify the flexibility of entry mode in China. Secondly, some of the findings are tentative and need future research effort. Data in the *structure* dimension during 1995-2003 is incomplete. In addition, data in the same dimension during 1980-1994 is scarce. As a result, "more flexibility" in the *structure* cannot be proved without condition. Thirdly, years divided in any of the two periods are too long. Thus, the trend embodied in the results is too general. At last, sample distribution in the two time sections is disproportionate. There are only 10 samples in the first section, while in the second, sample more than doubled to 24.

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Appendix

1. Nokia
2003 Merger
Industry: mobile telecommunications
Share of ownership: Nokia 60%

Name of Joint Venture	Time of Operation	Local Partners	Main Business
Beijing Capitel Nokia Mobile Telecommunications Co. Ltd.	1995	Beijing Capitel Co.Ltd.	Manufactures mobile telecommunications infrastructure systems and mobile phones
Beijing Nokia Hangxing Telecommunications Systems Co. Ltd.	1994	Beijing Hangxing Machinery Manufacturing Corporation	Manufactures Nokia digital mobile switching systems
Dongguan Nokia Mobile Phones Co. Ltd.	1995	Dongguan Nanxin Industrial Development Co. Ltd.	Manufactures advanced Nokia mobile phone products
Nokia (Suzhou) Telecommunications Co. Ltd.	1998 (wholly-owned venture) 2001 (joint venture)	Shanghai Alliance Investment Ltd.	Manufactures Nokia base stations and cellular network transmission equipment

Nokia Neu Comm Tech Company Ltd., China
- **Established 2000**
- **Software products research and development**
- **Partner NEU-ALPINE Software Holding Co. Ltd**

ChongQing Nokia Telecommunications Co. Ltd, China
- **Established 1998**
- **Provision of a full range of services, manufacture and supply of products for fixed networks**
- **Partners ChongQing Telecommunications Bureau, ChongQing PTAC**

2. IBM World Trade Corporation
Industry: computer
1980's Representative offices in Beijing and Shanghai
1992 Wholly-owned venture (IBM China Company Limited)
2000 Joint venture
IBM China Company Limited (IBM China) 70%
China Great Wall Shenzhen Co., Limited (Great Wall) 30%

3. 3Com Corporation
Industry: Internet protocol (IP) service and network service
2003 JV

3Com Corporation 49%
Huawei Technologies Ltd. 51%

4. Alcan Inc.
Industry: Aluminum
2002 JV
Alcan 50%
Qingtongxia Aluminum Company (QTX) 50%

5. Volkswagen
Industry: Automotive
1984 JV
Volkswagen 50%
SAIC 40%
CNAIC 10%

6. Mitsubishi Rayon Co., Ltd.
Industry: acrylic fiber
2003 JV
Mitsubishi Rayon Co., Ltd. 55%
Mitsubishi Corp. 10%
Itochu Corp. 10%
Marubeni Corp. 10%
Ningbo United Investment Holding Corp., Ltd. 15%

7. Benckiser
Industry: detergent
1996 JV
Benckiser 60%
Hubei Power 28 Company 40%

8. Victor Company of Japan, Ltd. (JVC)
Industry: deflection yokes
2000 JV
JVC 70%
Fujian Electronic Information Group (FEI) 10%,
Chunghwa Picture Tubes, Ltd. 10%,
Kuang Yuan Co., Ltd. (KYC) 10%

9. Bühler Machinery of Uzwil
Industry: manufacturer
1993 JV

10. Motorola
Industry: telecommunication
1987 representative office in Beijing
1992 wholly-owned venture (Motorola China Electronics Ltd.)

11. NEC

1989 JV (Tianjin NEC) Industry: machinery
1996 Wholly-owned venture (NEC China Co. Ltd) Industry: PC, semiconductor, TV
2002 JV Industry: manufacturing of TFT LCD panels and modules for PCs, Monitors and TVs
NEC 25%
SVA 75%

12. Toshiba Corporation
Industry: electronics
1995 joint venture (Shanghai Jinzhi Electronics Co., Ltd.)
Toshiba Corporation 40%
Shanghai Jinling Co., Ltd. 30%
Shanghai Cable Television Industrial Company 15%
Sunny Ocean Communication (H.K.) Ltd. 15%

13. Federal Express Corp. (FedEx)
Industry: express transportation
1999 JV (Federal Express-DTW Co. Ltd)

14. Matsushita Industrial Equipment Co., Ltd
Industry: manufacturing of welding materials
2002 JV
Kobe Steel Group. Kobe Steel, Ltd. 52%
Matsushita 25%
Tangshan Kaiyuan Electric Co., Ltd. 23%.

15. Kingston Technology Corporation
Industry: computer
2001 JV
Kingston Technology Corporation 80%
China Great Wall Computer Shenzhen Company Ltd. (CGCsz) 20%

16. Siemens
1990 JV in Beijing Beijing International Switching Systems Corporation (BISC)
1992 JV in Shanghai : Siemens Shanghai Medical Equipment (SSME)
1994 Wholly owned venture : Siemens China Ltd.
1995 in Xi'an : Siemens Signalling Company Ltd
1999 in Zhuzhou: Siemens Traction Equipment Co.Ltd.

17.GM
Industry: automotive
1997 JV
GM 50%
Shanghai Automotive Industry Corporation (SAIC) 50%

18. Honda Motor Co., Ltd
Industry: motorcycle production
2001 Merger
Honda Motor 50%
Sundiro 47.33%

Tianjin Motors Group Inc. 2.67%

19. Marconi
Industry:telecommunication
2000 Takeover of Nokia's JV
Majority share

20. Samsung
Industry: electronics
2001 JV
Samsung 49%
Shanghai Bell 51%

21. Rhodia
Industry: Chemistry
2001 JV
Rhodia 70%
Zhangjiagang Hengchang Chemical Company Ltd. 30%

22. Autoliv
Industry: Manufacturing
1995 JV
Autoliv 30%
Nanjing Hongguang Airborne-Equipment Factory 70%

23. BP
Industry: Oil
2002 JV
BP 40%
Sinopec 60%

24. HongKong Lika-shing
Industry:Medicine
2000 Acquisition of JV between Tongrentang, Hutchison and Jingtai
Hongkong Lika-shing 50%

25. Lonza
Industry: Chemistry
1999 JV
Lonza Majority share